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January 21, 1999

VIA HAND DELIVERY

Ms. Magalie R. Salas
Secretary
Federal Communications Commission
1919 M Street, N.W.
Room 222
Washington, D.C. 20554

RECEIVED

JAN 21 1999

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Re: Deployment of Wireline Advanced Telecommunications Service
Capabilities, CC Docket 98-147

Dear Ms. Salas:

Pursuant to Section 1.1206 of the Commission's rules, the Competitive Telecommunications Association ("CompTel"), by its undersigned counsel, hereby gives notice that on January 20, 1999, Russell Frisby, Joseph Gillan and the undersigned met with Commissioner Michael Powell and Paul Nagel, an intern to Commissioner Powell, to discuss the above-captioned proceeding. The attached materials summarize the presentation.

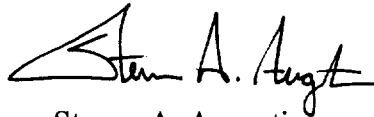
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KELLEY DRYE & WARREN LLP

Ms. Magalie R. Salas
January 21, 1999
Page 2

In accordance with Section 1.1206(b), an original and one copy of this notice is being provided.

Sincerely,

A handwritten signature in black ink, appearing to read "Steven A. Augustino". The signature is stylized with a large, sweeping initial "S" and a trailing flourish.

Steven A. Augustino

SAA:pab

Enclosures

cc: Commissioner Michael Powell
Kyle Dixon
Paul Nagle

A

RECEIVED

JAN 21 1999

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

An ILEC Affiliate is Only "Truly Separate" if the Affiliate Experiences the Same Incentives and Confronts the Same Barriers as Any Independent CLEC.

- I. The threshold requirement to ensuring that an affiliate is "truly separate" is substantial independent ownership.
 - A. Independent ownership establishes a fiduciary obligation to maximize the value of the CLEC affiliate as a stand-alone enterprise.
 - B. Restricting management compensation and stock options/bonuses to the performance of the publicly traded stock is necessary to appropriately align management incentives.
- II. If there is *any* significant common ownership between the affiliate and the ILEC, *all* inter-affiliate transactions must occur at cost-based rates available to any independent CLEC to prevent discrimination.
 - A. Common ownership permits any non-cost component in a transfer price between the ILEC and its affiliate to be offset when profits/losses are consolidated by the corporate parent.
 - B. Cost-based transfer prices are necessary to accurately reflect the real cost incurred by the corporate parent. ILECs should only be allowed to conduct cost-based transactions with their affiliates. An ILEC's CLEC should be limited to providing service using unbundled network elements (UNEs) purchased from the ILEC.
 - C. Section 251(c)(4) service resale by an ILEC affiliate is not a cost-based transaction and therefore should be prohibited. Service resale uniquely advantages the ILEC affiliate and is inherently discriminatory. Only an ILEC affiliate using service resale:
 - 1. profits from operating as an uncompensated marketing agent for the ILEC's access service.
 - 2. is unaffected by the inadequacy of the wholesale discount.
 - 3. benefits from the inability to differentiate its local services from those of the ILEC because it *wants* to be perceived as the incumbent.
 - D. The ILEC and its affiliate must be prohibited from joint marketing to assure independent behavior.



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B



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C



Why Separate Doesn't Mean Equal

The Case Against ILEC Affiliates for Advanced Services

By H. Russell Frisby Jr.

Here we are on the edge of the millennium, looking down at ... what? Every step is, essentially, a leap of faith, and regulatory decision-making increasingly relies on some sort of faith in a future that's pretty much like a pool of water: Safe, in and of itself, but unpredictable once gravity, velocity and other forces of physics—that is, the behavior of competing telecommunications carriers—are factored into the equation.

An examination of the Federal Communications Commission's (FCC's) proceeding on how to regulate the provision of advanced services by incumbent local exchange carriers (ILECs) underscores the risks associated with placing what the Competitive Telecommunications Association (CompTel) feels is a bit too much faith in the ILECs, and with underestimating the tendency of monopolies to expand and defend their status as monopolies.

The FCC has proposed allowing ILEC affiliates to provide advanced services free from ILEC regulation, including the local network opening requirements under Section 251(c) of the Telecommunications Act of 1996 as long as the affiliate meets certain structural separation and nondiscrimination requirements.

To maintain market share, the ILECs have every incentive to use any separate affiliate rules to avoid, through corporate structure, the market-opening obligations of the Telecom Act; indeed, BellSouth Corp. and other ILECs already are creating their own competitive local exchange carrier (CLEC) affiliates within their ILEC regions. The primary effect of a separate affiliate approach could be to foreclose entry by carriers that

plan to offer services that require anything more than a conditioned loop. If network facilities are shifted over to the affiliate (for example, through transfers or through new deployment), the only network elements available to competitors would be an aging plain old telephone service (POTS) network based on increasingly obsolete technology.

Section 251(c) of the Telecom Act was written precisely to eliminate the barriers that continue to prevent the CLECs from competing. According to CompTel, "If the only way to tap into the mass market for advanced services is to enjoy the economies of the ILECs' existing networks, it contradicts public policy to reserve that access only for the ILEC." Section 251(c) expands access to these capabilities and makes the provision of advanced services more feasible for all carriers.

The putative benefits of embracing a separate affiliate approach to permitting the ILECs to provide advanced services can be, and often are, overstated. First, there is no evidence to support the ILECs' contention (and the FCC's assumption) that a separate affiliate's use of unbundled network elements (UNEs) will be representative of the way that CLECs use UNEs. The mere existence of a separate affiliate is insufficient to ensure that an ILEC offers UNEs in full compliance with Section 251(c); for example, an ILEC affiliate might provide

services through physical collocation arrangements and subsequent entrants could find themselves precluded from such arrangements because all available collocation space is exhausted.

If the FCC insists on pursuing a separate affiliate approach that defines an affiliate as truly "separate," its proposed separation requirements should be strengthened in the following manner:

- **Joint Ownership.** The ILEC and its affiliate should be prohibited from jointly owning any facilities or equipment (not just switching equipment), and from jointly owning any real property (not just the land or buildings in which switches are located). In addition, nontelecommunications functions and services should be made available on a nondiscriminatory basis.

- **CPNI.** Access to the ILEC's customer proprietary network information (PNI) should be provided on a nondiscriminatory basis.

- **Transfers of Assets.** Any transfer of assets to an affiliate should subject the affiliate to ILEC regulation. Thus, the ILEC should be prohibited from transferring any assets, including customer accounts, equipment, employees and brand names. Any use by an affiliate of a brand name similar to the ILECs' should be deemed a transfer of the name.

In addition, the FCC should consider expanding its proposed rules to include the following requirements:

- **Compliance Plan.** Before offering advanced services through an affiliate, an

ILEC must submit a detailed plan showing how the proposed affiliate satisfies each of the separation requirements adopted in the commission's proceeding.

- **Substantial Independent Ownership.** The FCC should require that an ILEC affiliate have a substantial percentage of its ownership—at least 40 percent—be held by people or entities not affiliated in any way with the ILEC parent. This is critical to creating an entity that operates independently of the ILEC.

- **UNE Use Requirement.** The affiliate should be required to obtain access to the ILEC's network on a UNE basis, and should be prohibited from reselling the ILEC's end-user services. Use of UNEs is the only way that a separate affiliate structure can improve the availability of network elements to competitors.

- **Joint Marketing Ban.** The FCC should bar the ILEC and its affiliate from engaging in joint marketing or advertising of any kind. Joint marketing or advertising undermines the separation between the affiliate and the ILEC.

It is worth pointing out that the FCC's separate affiliate approach roundly was

condemned not only by competitive carriers and state regulators, but by the ILECs themselves. Ironically, the ILECs' own comments to the FCC in its proceeding betray their complete awareness of the advantages they wield over local competitors.

US WEST Inc., for example, contended that the ILECs are "uniquely well-positioned" to offer such services because their networks "reach into virtually all communities" and because such networks "will permit economies of scope in the rollout of packet-switched technologies." US WEST even admitted candidly that "having to pay" its own inflated loop prices "has deterred CLECs from deploying services in smaller and more rural areas."

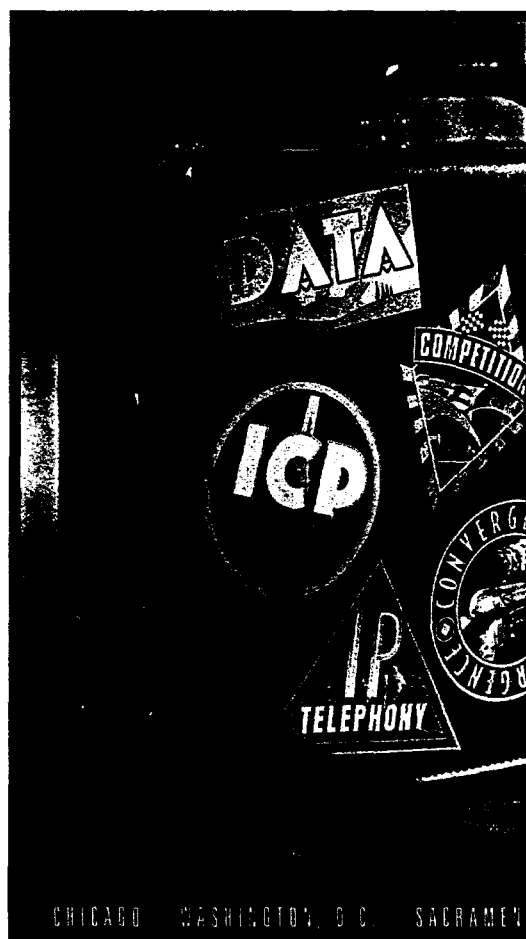
Moreover, a separate affiliate approach requires vigorous enforcement and rigorous monitoring. Therefore, it is somewhat surprising that the FCC would propose taking on this much work, given its myriad and complex responsibilities such as driving access charges to cost, reforming universal service support mechanisms, reviewing telecommunications industry mergers and reviewing the Bell operating companies' (BOCs') Section 271 interLATA (local access

and transport area) entry applications.

There is nothing to be gained—and much to be lost and wasted—in reinventing the wheel. CompTel believes that the only sensible approach for the FCC to take with respect to regulating the ILECs' provision of advanced services is to clarify, enforce and broadly apply Section 251(c) of the Telecom Act. This approach recognizes that the key to any rapid, widespread deployment of advanced services is cost-based, nondiscriminatory access to the ILECs' networks.

The separate affiliate approach—without the proper safeguards in place—puts the competitive industry at risk. A professional high diver never takes a leap without knowing how deep the water is. With respect to advanced services, the FCC's proposed separate affiliate rules offer competitors only the shallowest protection. X

H. Russell Frisby Jr. is president of the Competitive Telecommunications Association (CompTel). Based in Washington, CompTel is the principal industry association for competitive telecommunications carriers and their suppliers. For more information, visit CompTel at www.comptel.org or call (202) 296-6650.



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